DIRECT LOANS

TRUE/FALSE TEST

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☑ ❑ 1. *Direct Loans provide "local control" to participating schools.*

Schools decide how much administrative responsibility they wish to assume, determine the division of work between financial aid and business offices, and decide how they carry out their day-to-day operations.

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❑ ☑ 2. *Direct Loan schools have to hire additional staff and incur major costs in converting to a new way of operating.*

Virtually none of the schools participating in Direct Loans in 1994-95, the Program's first year, report that they had to add staff in either the financial aid or the business office. Most schools that plan to add staff in the future reported understaffing before joining Direct Loans.

Most schools report minimal equipment purchases — typically for a new PC or high-speed printer. Although some Direct Loan schools chose to upgrade their entire systems, involving significant equipment costs, these onetime purchases were long planned for and driven by the need for improvements in both their financial aid and business office operations regardless of their Direct Loan participation.

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☑ ❑ 3. *There is no greater liability risk in participating in Direct Loans than there is in any other Title IV student financial aid program.*

The Department's Office of General Counsel has carefully researched this frequently-raised issue and determined that the liability for schools participating in Direct Loans is no greater than that which exists for schools participating in any other Title IV student financial aid program. Two "Dear Colleague" letters on this issue are available from the Direct Loan Task Force, one published in January 1995, and the second published in July 1995.

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❑ ☑ 4. *Schools have to assume many duties such as credit checks, collections, and loan servicing previously performed by banks.*

Under Direct Loans, the Department of Education, through contracts with private companies, performs credit checks on PLUS borrowers, services, and collects all loans. Schools bear no responsibility or cost for these duties.

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☐ ☑ 5. *The Department of Education can give out money but it has no track record for collecting money.*

The Department of Education has been collecting defaulted student loans for decades. During the past four years, the Department's collection efforts have improved dramatically. Annual collections on loans held by the Department increased fivefold from FY 1992 to FY 1995, from $98 million to $605 million. During the same period, collections through Federal income tax refund offsets exceeded $2 billion.

In addition, the Department has already collected approximately $70 million under Direct Loans. Direct Loan borrowers are sent quarterly statements of interest accrual and given the option each quarter to pay the interest in order to avoid larger payments later.

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☐ ☑ 6. *The Direct Loan Program is a haven for schools with high default rates.*

Institutional eligibility to participate in Direct Loans is the same as institutional eligibility to participate in the FFEL Program. Therefore, if a school's cohort default rate exceeds 25% for three consecutive years, the school is ineligible to participate in either Direct Loans or FFEL. The average FY 1992 cohort default rate for schools participating in Direct Loans is 11.3%, compared to 15% for all schools participating in the FFEL Program.

Schools must continue to maintain their eligibility for the FFEL Program even after they begin participating in Direct Loans. Year one Direct Loan schools will be covered by the FFEL default rate through FY 1996; year two schools will be covered through FY 1997. The Department published regulations in December 1995 to set out the calculation of default rates and how these rates will be used to determine a school's eligibility to participate in the Direct Loan and FFEL Programs.

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☑ ☐ 7. *Direct Loans is designed to reduce defaults by providing borrowers with information, better service, and repayment flexibility throughout the life of the loan.*

Lack of service and responsiveness on the part of lenders, secondary markets, and loan servicers are two of the problems most often reported by FFELP borrowers. FFEL loans are typically sold (sometimes several times) and borrowers frequently report confusion about just where to send payments, deferment forms, and requests for forbearance. Direct Loans provides borrowers with a single entity for communication from the first disbursement of the loan until all of a borrower's Direct Loans are paid in full. Furthermore, a variety of repayment options are available to Direct Loan borrowers who also have the flexibility to change repayment plans as their financial and personal situations change.

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☐ ☑ 8. *Direct Loans will create more "big government" as it takes over the FFEL Program, a private program.*

The FFEL Program is not a private program. Taxpayers pay billions of dollars annually to lenders, guarantee agencies, secondary markets, and servicers to subsidize the cost of this program. Without these subsidies, this "private" program would cease to exist. Most of the work in the Direct Loan Program is performed by the private sector under contract with the Department. The Department projects that 80% of Direct Loan and FFEL transition funding will go to private companies; only 5% will actually be used to support Federal employees.

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☐ ☑ 9. *Reconciliation is a nightmare and will cause nothing but problems for schools.*

The Department has reconciled and closed out 99 percent of all the transactions processed for the 1994-95 academic year. This means that the Department has nearly closed out the first year of operation within six months of year-end — a significant achievement never before equaled by any Federal student aid program.

Reconciliation of cash has never been a problem in Direct Loans. In fact, an independent audit performed by the accounting firm of Urbach, Kahn and Werlin gave the Direct Loan Program a "clean" audit opinion — the first time ever for a Federal student aid program! The matching of individual data records is the activity that has been problematic for some schools in the first year of the program. The Department continues to work with participating schools to streamline this process.

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☑ ☐ 10. *The Department of Education provides Direct Loan schools with the assistance and support they need to successfully implement this program on their home campus.*

Schools have given the Department high marks for the responsiveness the Department has shown throughout the entire implementation effort. The Department made a commitment to provide the highest quality customer support and technical assistance to all participating schools. Software, training, program materials, and technical and program assistance, both on and off site, are provided free by the Department of Education. Direct Loan schools are not charged for their data transmission costs, including those costs related to obtaining student data through the Central Processing System. Also, toll-free telephone lines have been established to ensure that students and schools have ready access to the advice, assistance, and help they might need.

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❑ ☑ 11. ***The Department of Education has gone beyond its statutory authority and created an "unlevel playing field" in its competition with the FFEL Program.***

The authorizing legislation for Direct Loans does not require the Department to create a "level playing field" with the FFEL Program. Within statutory guidelines, the Department designed the Direct Loan Program to maximize benefits to the borrower and streamline processes for the school. Many of the differences between the Direct Loan and FFEL Programs stem from the basic structural differences in the programs themselves.

Current law requires an orderly transition from the FFEL Program to the Direct Loan Program. If Congress decides to change current law and establish a true "level playing field," the Department would support changes such as shifting the entitlement under the FFEL Program from guarantors and lenders to borrowers; allowing FFEL borrowers to change repayment plans without penalty; requiring lenders to charge the same interest rate to all borrowers; allowing the Department of Education to offer discounts to borrowers who make timely repayments; and ensuring that FFEL borrowers will only have to deal with one entity for all their loans throughout the life of the loans.

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❑ ☑ 12. ***Borrowers at schools that choose to go into Direct Loans are at a disadvantage because they will have both FFEL and Direct Loans to repay.***

Direct Loan borrowers who also have FFEL Program loans can easily consolidate these loans into the Direct Loan Program. And, the borrower will not lose any benefits by doing so. Direct Consolidation Loans are designed to maximize the terms and benefits to the borrower. In 1995-96, students at Direct Loan schools will be able to consolidate their FFEL loans into Direct Loans while they are in school, further easing the transition from one program to the other.